No. 347

IN THE

Supreme Court of the United States

..... TERM, 1945

F. H. McGRAW & COMPANY, INC.,
Plaintiff-Petitioner,

v.

JOHN T. D. BLACKBURN, INC., and MILCOR STEEL CO.,
Defendants-Respondents,

and

THE AETNA CASUALTY & SURETY COMPANY,
Third Party Defendant-Petitioner.

PETITION AND BRIEF FOR A WRIT OF CERTIORARI

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PETITION FOR A WRIT OF CERTIORARI

To the Honorable Chief Justice and Associate Justices of the Supreme Court of the United States:

The petitioners, F. H. MCGRAW & COMPANY, INC. and THE AETNA CASUALTY & SURETY COMPANY, respectfully pray for a writ of certiorari to review a decree of the Circuit Court of Appeals for the Second Circuit, entered on May 22, 1945, affirming a judgment entered by the United States District Court for the District of Connecticut in favor of the respondent, John T. D. Blackburn, Inc. against the petitioners, for the sum of $9,009.64, with interest and costs *(R., 619-620).

* (R.) with a numeral indicates a page reference to the transcript of the record in the Circuit Court of Appeals.

Summary Statement of Matters Involved

F. H. McGraw & Company, Inc., a New Jersey company engaged in business as a general contractor and builder in the State of Connecticut, received a contract from the State of Connecticut, on or about August 16, 1938, for the general construction of the Continued Treatment Units, Fairfield State Hospital, at Newtown, Connecticut (R., 109; 599). In connection therewith, and as required by Connnecticut Statute [§540d (r), Conn. General Statutes, Supp. 1937; §786e (r), Supp. 1939], it filed a surety bond, executed by itself as principal and The Aetna Casualty & Surety Company as surety (R., 110-112; 599-600). By the terms of the Statute, as well as of the instrument itself, the bond was to be held by the Connecticut Commissioner of Public Works for the use of each party who shall have "furnished materials or supplies or performed labor in the prosecution of the work * * *, and *who has not been paid therefor*" (§540d (r), Conn. Gen. Stat., Supp. 1937; §786e (r), Supp. 1939; R., 111; 600).

On or about September 1, 1938, McGraw entered into a written subcontract with the Sherman Plastering Co. Inc., a New York company, whereby the latter company undertook to perform certain work and furnish certain materials to McGraw's Newtown project (R., 109; 600-601). Sherman, which finished its contract on January 10, 1940 (149 Fed. (2), 301, * 303), purchased some supplies for that project from John T. D. Blackburn, Inc., also a New York company, from July 19, 1939 to January 9, 1940 (149 Fed. (2), 301, 304; R., 602). During that time, and between those dates, Sherman made substantial payments to Blackburn, having received from F. H. McGraw & Company, Inc., on account of its contract, the sum

* Reporting the opinions of the Circuit Court of Appeals herein.

of $77,195.76 prior to January 10, 1940 (149 Fed. (2), 301, 303; R., 313-314). The Trial Court found that the payments made by Sherman to Blackburn between July 19, 1939 and January 9, 1940 were made as payments on account of Sherman's indebtedness, without direction or instruction (Finding #20, R., 603). The Trial Court further found that Blackburn credited the payments which it received from Sherman on Sherman's running account of indebtedness "without making any allocation of any of said payments to any particular job" (Finding #21, R., 603). He also found that:

> "If the payments described in Paragraph 20 be deemed all applied against the earliest sales made by Blackburn to Sherman then unpaid, Sherman's indebtedness to Blackburn on account of material furnished for the Fairfield job* was fully paid and discharged" (Finding #22, R., 603-604).

and that:

> "There is no proof that prior to January 22, 1940, Blackburn manifested an intent to apply the several payments theretofore made by Sherman to Sherman's indebtedness of specific sales of material used elsewhere than in on account the Fairfield job * * *" (Finding #23, R., 604).

Sherman's other jobs, to which the Trial Court referred, were jobs which had nothing to do with McGraw or McGraw's Newtown project. They were all commenced *after* January 9, 1940, the date of Blackburn's last delivery of materials to the McGraw's Newtown job. It is undisputed that the only unpaid indebtedness which existed between Sherman and Blackburn *prior* to January 9, 1940, when the payments involved herein were received

*. The terms "Fairfield job" or "Fairfield project" and "Newtown job" or "Newtown project" have been used interchangeably in the opinions and briefs below.

by Blackburn from Sherman, was Sherman's indebtedness on the Newtown job (149 Fed. (2) at 308-309). Subsequent to January 9, 1940, Sherman started jobs at Coxsackie, New York; Dannemora, New York; Bedford Hills, New York; and Beacon, New York (R. 580, Exh. M-50; R. 552, Blackburn's Exh. 22). All of Blackburn's deliveries to those new jobs were made after January 9, 1940, the date of Blackburn's last delivery to the Newtown job. With the exception of two small deliveries made to Coxsackie on January 12, 1940 and January 19, 1940, everyone of Blackburn's deliveries to the Coxsackie, Dannemora, Bedford Hills and Beacon jobs was made *after* January 24, 1940 (R. 580, Exh. M-50; R. 552, Blackburn's Exh. 22), the date when Blackburn allegedly manifested an intent to re-apply the monies which it had received from Sherman between July 19, 1939 and January 9, 1940 to the jobs other than the Newtown job.

Upon the basis of Blackburn's alleged re-application of the payments received long before January 9, 1940, when the only existing indebtedness was the indebtedness on the Newtown job, to obligations incurred by Sherman long after January 9, 1940, on jobs which were not in existence or even contemplated when the payments were received, Blackburn filed a claim in the Connecticut District Court against the petitioners upon their bond, contending that, under the Connecticut statute, it was a party "who has not been paid" for its Newtown deliveries. The initial proceedings had been commenced by McGraw under the Federal Interpleader Act, 28 U.S.C.A. 41 (26), against Sherman's claimants, including Blackburn, the basis of jurisdiction being the diversity of citizenship of the various parties.

Blackburn's claim was sustained by the District Court and a judgment entered in its favor for the full amount thereof (R., 619-620). The Trial Court ruled that Blackburn had complied with the condition precedent specified

in the Connecticut statute that it be a party "who has not been paid therefor" because, *under New York law,* Blackburn was empowered to switch the payments which it had received from Sherman between July 19, 1939 and January 9, 1940 and which, upon its books, had extinguished Sherman's obligation for the Fairfield deliveries, to obligations incurred by Sherman upon other jobs long after January 9, 1940 which were not in existence or even contemplated when the payments were originally received, thereby reviving the previously extinguished obligation of McGraw and the surety upon the statutory bond. The basis for the District Court's judgment was the supposed provisions of the New York law (R., 607-612). No reference whatsoever was made by the District Court to a single Connecticut authority or decision (Cf., *Klaxon Co.* v. *Stentor,* 313 U. S. 487, 496; *Griffin* v. *McCoach,* 313 U. S. 498, 504).

The Circuit Court of Appeals disagreed with the Trial Court's decision that the New York law applied, declaring that, under *Erie Ry. Co.* v. *Tompkins,* 304 U. S. 64, and kindred decisions, the Trial Court was required to apply the law of Connecticut to the facts of this case (149 Fed. (2), 301-305). Nevertheless, the Circuit Court affirmed the judgment in favor of Blackburn by ruling that, under *New York law,*(!) a letter from Blackburn to McGraw dated January 24, 1940, stating that its Newtown deliveries were unpaid, was sufficient to establish a legally operative intention to apply the payments made by Sherman between July 19, 1939 and January 9, 1940 to its deliveries on Sherman's other and subsequent jobs (149 Fed. (2), 301, 305-307). It brushed aside the petitioners' contention that, under Connecticut law, the principle of allocation of payments invoked by the Circuit Court, does not and cannot apply where, as here, only one indebtedness, *i.e.,* the Newtown indebtedeness, existed when the payments were received by Blackburn, that the Newtown

obligation was instantly discharged as a matter of law at that time that the payments were received; and that the debt could not be subsequently revived, by a cancellation of the payments, solely for the purpose of imposing an obligation upon McGraw and Aetna under their bond (149 Fed. (2) at 305, footnote 1).

The petitioners moved for a rehearing in the Circuit Court of Appeals wherein they emphasized the fact that the Circuit Court's decision upon this aspect of the cause was neither the law of the State of Connecticut nor the State of New York, nor, indeed, supported by the common law of any of the states of the union, the common law of England or the Roman Civil law from which the doctrine of allocation of payments was obtained. Two opinions were rendered by the Circuit Court of Appeals upon the petition for a rehearing; an opinion by Circuit Judge Clark reaffirming his prior position, and an opinion by Chief Judge Hutcheson vehemently dissenting therefrom (149 Fed. (2), 307-309). The third member of the Court, Judge Simons, apparently took no position upon the rehearing.

Judge Clark based the judgment of the Court squarely upon "the power of debtor and creditor to make their own agreement of allocation", under New York law, even though it resulted in an allocation of the payments to an obligation or claim which did not exist at the time that the payments were received, thereby subjecting the principal and surety upon a Connecticut statutory bond, to a liability for a debt which had already been discharged (149 Fed. (2), 307). Chief Judge Hutcheson refused to accept the proposition: "that Blackburn was a creditor whose claim was unpaid, when, as I read the record, the Newtown claim was paid and was later revived by agreement between Blackburn and Sherman. I think Judge Hincks finds as much, but he seems to believe that nobody

had anything to say about the application except debtor and creditor. I can't agree with him" (149 Fed. (2) at 308, footnote 1). The foregoing statements, declared the Chief Judge, were embodied in his original memorandum to the Court, when the case was first under consideration (149 Fed. (2) at 308).

In his opinion upon the petition for a rehearing, after referring to "that master darkener of counsel, my brother from Connecticut, with his firm footed statement of New York law" (p. 308), Chief Judge Hutcheson declared (pp. 308-309):

> "I only know that I turned aside from the sole and simple issue on which the decision rightly turned, whether Blackburn was, under the Connecticut statute, 'a party who * * * shall have furnished material or supplies * * * *and who has not been paid therefor*' (emphasis supplied), and, stumbling, lost my way. Then it happened to me, as it had to another and worthier Joseph, that my brethren 'said one to another, 'Behold, this dreamer cometh,' and they stripped me out of my coat, my coat of many colors, my wondrous judgment intuitive, the feeling which is the triumphant precursor of the just judgment, and cast me into a pit, a pit empty and full of darkness. But convinced against my will, I was of the same opinion still, and, reflecting on the admitted facts that 'all of the deliveries by Blackburn to the Newtown job were made between July 19, 1939, and January 9, 1940, that the moneys paid by Sherman to Blackburn during that period were sufficient to cover Sherman's indebtedness on that job', and that the Coxsackie job on which Blackburn and Sherman attempted to reapply the payments did not come into existence until January 24, 1940, I wondered why my original impression, that Blackburn was not a supplier whose claim was unpaid, was not right, and, wondering, moved groping toward the light. When then appellant, still on the Orlando

furioso side, but this time concentrating on the accepted fact that the critical payments to Blackburn discharged the Newtown indebtedness before the Coxsackie indebtedness came into being, filed its petition for rehearing, my darkness became light, and I saw face to face what before I had seen through a glass darkly, that 'the principle of allocation or appropriation of payments invoked by this court simply does not exist'. As appellant in the petition for rehearing very well states, 'A creditor who receives a payment from his debtor, without direction, at a time when only one debt exists, *has no choice,* no *right to allocate,* no *power to elect.* He must apply it upon the existing debt, and the law will do so even if he does not. By that application of law, the debt is *instantly* discharged upon the creditor's receipt of the payment'. Having been discharged, the debt could not be revived so as to make Blackburn, under the Connecticut statute, a supplier whose debt had not been paid. The error in the approach of the district judge and of the majority lies in the fact that they have assumed, contrary to the undisputed proof, that, when the critical payments were made by Sherman to Blackburn, there was in existence a running account of more than one debt, and Blackburn, having an option to apply the payment to one or the other of those debts, could exercise it in a reasonable time. I agree with the district judge, and with the majority, that the contract between Blackburn and Sherman was a New York contract, that the payments were made in New York, and that the law of New York determines whether or not Blackburn was a supplier whose debt had not been paid. I think it perfectly clear, though, that under the law of New York, as declared both in the Connecticut and the New York decisions, and as is the rule generally elsewhere, there being only one debt to which the payments could be applied when they were received by Blackburn, it was discharged. Having thus been fully paid, Blackburn could not, by an arrangement between him and the debtor,

again become, for the purpose of asserting a statutory liability against the surety, a person whose debt had not been paid. Looked at as the undisputed facts require it to be seen, this is a case where the debtor having fully paid the creditor, creditor and debtor, in order to assert a statutory liability against a surety, have undertaken to cancel the payment and revive the debt. So looked at, the case presents no difficulty either in law or in morals. The fallacy in the majority opinion lies, I think, in its failure to recognize the force of the admitted facts shown by plaintiff's exhibit 22, 'Sales made by Blackburn to Sherman Plastering Co.', that from June 29, 1939, to Jan. 24, 1940, when the Coxsackie job commenced, the moneys Sherman had paid in had completely discharged the debts then due, and that the Sherman-Blackburn arrangement was not an allocation of payments, not yet applied, but a cancellation of payments made in discharge of the Newtown debt, and their application to a debt created after that discharge. This, as between themselves, of course they could do, but they cannot do it as to the surety. I think it clear that the petition for rehearing as to Blackburn should be granted and the judgment in his favor reversed.

Jurisdiction of the Court

This application is made under Section 240 of the Judicial Code (28 U.S.C.A. §347).

The Issues Presented by this Petition

The within petition presents the following issues:

(1) That, under the Connecticut law which the Circuit Court was required to apply, *Erie Ry. Co.* v. *Tompkins*, 304 U. S. 64, the Circuit Court erred in ruling that a creditor who has received a payment from his debtor, without direction, at a time when only one indebtedness existed between them, possessed the right to cancel that

payment and re-apply the same to a subsequent indebtedness which did not exist at the time that the payment was received or the alleged allocation made, in order to enforce a statutory liability against the principal and surety upon a Connecticut bond as a party "who has not been paid" the amount of the discharged indebtedness.

(2) That, in deciding whether Blackburn was a party "who has not been paid therefor", *i.e.*, whether Blackburn had complied with the express condition precedent to the liability created by the Connecticut statute, the Circuit Court erred in ruling that the issue was to be determined by New York law. In refusing to hold that Connecticut law governed the question of Blackburn's compliance with the statutory condition precedent to the petitioners' liability upon a Connecticut bond required by a Connecticut statute, executed, delivered and performable in Connecticut, covering a Connecticut public work and deliveries of material in Connecticut, the Circuit Court of Appeals erroneously ignored the full faith and credit clause of the Constitution, as well as the doctrine of *Erie Ry. Co.* v. *Tompkins, supra.*

Reasons for the Allowance of the Writ

(1) The questions presented by this petition are of vital importance in the law governing the execution, interpretation, performance and enforcement of surety bonds required by statutes governing public works and public construction. If a materialman may, at any time that he pleases, cancel a payment for materials which he has delivered, at a time when such indebtedness constitutes the only indebtedness from his vendee, in order to re-apply the monies to a subsequently accrued obligation for the sole purpose of reviving the liability of a surety upon its bond, a startling change will have been effected in the settled law of centuries, opening the door to the grossest

of frauds and impositions. It was not the province of the Circuit Court to formulate new law for the State of Connecticut. It was obligated, under *Erie Ry. Co.* v. *Tompkins,* 304 U. S. 64, and kindred decisions, to apply the law of the State of Connecticut to the facts of the instant case. Its failure to do so necessitates a review of its determination by this Court.

(2) Of equal, if not greater, importance is the question of whether or not the State and Federal Courts are required by the full faith and credit clause of the Constitution, when called upon to enforce a statutory liability created by a sister State, to apply the law of the creating State in order to determine whether the conditions precedent to the statutory liability have been fulfilled. In this case, the State of Connecticut created a statutory right which had never existed before for the benefit of materialmen upon Connecticut public projects, circumscribing that right by attaching thereto the express statutory condition precedent that the only party who can avail himself of the statutory benefits was a party "who has not been paid therefor." By its decision that Blackburn was entitled to enforce the bond against the petitioners as a party "who has not been paid therefor" because it would be so considered, under New York law, *although under Connecticut law, it would be deemed fully paid,* the Circuit Court of Appeals ignored the full faith and credit clause of the Constitution and expanded the liability created by the Connecticut statutes for the benefit of non-residents and non-citizens of that State. The power of a State or a Federal Court to thus extend a State-created right, for the benefit of non-residents and non-citizens, under a set of facts which would have resulted in a denial of any recovery by the Courts of the creating State to its own citizens and residents, is an issue of such immense public importance that a review of the Circuit Court's decision

should be entertained by this Court (*Guaranty Trust Co. v. York,* 65 Sup. Ct. 1464, June 18, 1945).

WHEREFORE, Petitioners respectfully pray that a writ of certiorari issue to the United States Circuit Court of Appeals for the Second Circuit, commanding said Court to certify and send to this Court for its review and determination, on a day certain to be named therein, a full and complete transcript of the record and all proceedings in the case numbered on its docket 147, and that said decree of the United States Circuit Court of Appeals for the Second Circuit, affirming the judgment obtained by John T. D. Blackburn, Inc. against the petitioners, be reversed by this Honorable Court, and that Petitioners have such other and further relief in the premises as to this Honorable Court may seem just.

Dated, August 16th, 1945.

F. H. McGRAW & COMPANY, INC., and
THE AETNA CASUALTY & SURETY COMPANY,
By JOSEPH LOTTERMAN and
LOUIS A. TEPPER,
Counsel.